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I.R.S. Going After Businesses on Withholding Tax
By DAVID CAY JOHNSTON

The Internal Revenue Service plans to announce next week that it is actively pursuing small-business owners who are bragging on the Internet and in seminars that they do not withhold taxes from their employees' paychecks, arguing that the tax laws do not apply to them.

Dale Hart, the I.R.S. deputy commissioner for small businesses and the self-employed, said the agency was now looking for business owners who have stopped withholding and turning over income, Social Security and Medicare taxes, and was "stepping up" the pressure on them.

Workers at these companies, who Mrs. Hart said "are being scammed by their bosses," will also be pursued and will be assessed penalties unless they send in the taxes that should have been withheld from their paychecks.

Some of the business owners, as well as the promoters who advise them, will be prosecuted for tax evasion and other crimes, said Mark E. Matthews, chief of the I.R.S. criminal investigation division. Indictments may take months.

In addition, the agency has tightened its procedures for issuing refunds to business owners who say they are exempt from the tax laws, said John Buchanan, the I.R.S. executive responsible for ferreting out sham trusts and similar commercial tax evasion schemes.

The changes, and an effort to encourage workers to turn in bosses who stop withholding taxes, come as proponents of theories that the tax laws are a hoax prepare to meet in Washington.

The New York Times reported in an article on Nov. 19 that at least 23 small-business owners had publicly declared on the Internet that they did not withhold taxes from their workers' paychecks. These owners told The Times that the I.R.S. was making no effort to make them pay.

One company named in the report, the Kristi Tool Company of Magnolia, Mass., advertises that it has not withheld taxes since 1979. Its owner, Dick Celata, said in an interview that the I.R.S. had never tried to make him pay and he said he took that as proof that he was correct in his belief that he was not required to pay taxes.

In recent weeks Dick Simkanin, owner of Arrow Plastics in Bedford, Tex., who maintains a Web site with the names of businesses that say they do not withhold taxes, has added three more businesses to his list.

Another business, Jon Peters Plumbing in Omaha, said it stopped withholding nine years ago. The Candleberry Creek Company in Cheona, Ill., stopped withholding in 1998.

Frank Keith, the senior I.R.S. spokesman, said in November that "with limited resources the I.R.S. must often choose which cases to pursue" and that it focused on those that would generate the most revenue.

Several former I.R.S. commissioners, as well as tax policy officials who had served in both Republican and Democratic administrations, said at the time that they were shocked at the failure of the I.R.S. to move against these business owners and warned that unless enforcement action was taken swiftly the movement would grow, threatening the integrity of the income tax system.

Days before the article was published about 60 business owners gathered in Huntington Beach, Calif., at the invitation of Nick Jesson, owner of N.T.D. Electronics in Huntington Beach, to plan strategies to expand their movement.

Next Saturday hundreds of people, including business owners, are expected to meet at the Hilton Hotel in Arlington, Va., to discuss ways to "expose and end the illegal operation of the income tax system," according to the event's sponsor, Robert L. Schulz of the We the People Foundation in Queensbury, N.Y. Among the tactics urged by some of those who have announced they will attend is persuading more business owners to stop income tax withholding, which is the source of more than 80 percent of federal income tax, Social Security and Medicare revenues.

Mrs. Hart, the I.R.S. deputy commissioner, said that arguments like the one that asserts that the income tax applies only to foreign-owned companies operating in the United States are "frivolous claims that have no legal authority" and have been thoroughly rejected by the courts.

But she said the agency had concluded it must conduct a public education program, especially for "poorly educated workers" who may tend to accept statements by their employers that income taxes are voluntary.

She said that while penalties would be assessed against workers who fail to turn over taxes that should have been withheld from their paychecks, an exception might be made for workers who pay but do not file promptly or pay less than they owe.

"We would have to consider that on a case-by-case basis," Mrs. Hart said.

The agency has also tightened scrutiny of requests for withholding tax refunds, said Mr. Buchanan, the I.R.S. executive assigned to police commercial evasion schemes.

Two companies that do not withhold taxes, Bosset Partners Marketing in Clearwater, Fla., and N.T.D. Electronics, said the I.R.S. promptly refunded more than \$200,000 in withholding tax refunds when they asked for their money back.

Mr. Buchanan said the I.R.S. had tightened procedures for processing withholding tax refund claims.

"We have pretty good filters to intercept these refund requests and only a handful are getting through," he said. "And those that do get through we are finding posthaste afterward because we now have a mechanism in place" to identify such errors.